

Trade Policy as Trust Building in the Korean Peninsula

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September 28, 2013

Executive summary

In his August press conference, Minister for Unification Ryu Kihl-jae developed three dimensions of President Park Geun-hye's 'trust politik' for the Korean peninsula: enhanced communication, security and international aid to infrastructure. Few observers would contend that building infrastructure is essential in the case of North Korea. But, the experience of international aid in this domain is very mixed if aid projects are defined with too little attention to the international environment of the recipient, in particular to its trade potential. This paper pleads for adding a trade policy dimension to Minister Ryu Kihl-jae's program.

The paper proceeds in five steps. First, it argues that, despite the appearances, it is not premature to open a debate on trade policy—a topic which, at a first glance, sounds mundane in the current circumstances so much dominated by denuclearization. This is because trust-building requires debates on concrete actions—which ones, in which order, at which conditions, etc. Second, the paper examines key constraints on the trade policy to be designed: it should help to diffuse political tensions; it should take into account the profound lack of knowledge of the strengths and weaknesses of the North Korean economy in the world economy; it should be frugal in institutions since it will take time to build them in North Korea.

The three last sections examine three options which meet these constraints. The first one is a fast transition inspired by the very successful trade policies of the Baltic countries (Estonia, Latvia and Lithuania) which happen to be the most appropriate references for North Korea. The second option is a more progressive transition inspired by the successful policy of Chile, and combined with a systemic use of Free Economic Zones. The third option is the conclusion of a free trade agreement or a custom union between North and South Korea. This third option is both a follow-up of the first or second option, and a step towards the reunification of the Korean peninsula.

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Introduction

In his August 21st press conference, Minister for Unification Ryu Kihl-jae developed three dimensions of President Park Geun-hye's 'trust politik' for the Korean peninsula: enhanced communication, security and international aid to infrastructure. Few observers would contend that building infrastructure is essential: North Korea lacks infrastructure to an extent rarely observed in the rest of the world. That said, the experience of international aid in this domain is very mixed. Very often, such aid has been wasted in inadequate projects. There is thus a need to look at the key conditions which will make such aid beneficial for all the North Koreans—not only for the foreign contractors or for the North Korean intermediaries.

A key reason of wasted international aid is that aid projects are defined with too little attention to the international environment of the recipient—in particular to its trade potential. This mistake is even more frequent and costly when the aid receiver is initially a very closed and distorted country. For instance, the 24 years of Saddam Hussein's regime has ruined Iraq's economy by imposing increasingly tight and distortive regulations (quotas, licenses, public distribution system, etc.) which have fuelled rents and corruption. But, after Saddam Hussein's fall, the successive administrations and governments did not try to open the Iraqi economy as soon and as widely as possible, rather keeping most of the existing distortions in place, adding new ones [World Bank 2010] and letting the process of Iraq's accession to the WTO going nowhere (no activity reported since 2010 [WTO website]).

As a result, this paper pleads for adding a trade policy dimension to the infrastructure aid component of Minister Ryu Kihl-jae's program in order to ensure the use of international aid into the most productive North Korean activities. This suggestion echoes South Korea's

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experience: the international aid received by South Korea did not substantially boost its domestic economy (while fuelling corruption) until the early 1960s, when the country embarked on a very successful export-led policy [Krueger et al. 1989].

The paper is organized as follows. Section 1 argues that, despite the appearances, it is not premature to open a debate on trade policy—a topic which, at a first glance, sounds mundane in the current circumstances so much dominated by denuclearization—because trust-building requires debates on concrete actions. Section 2 examines the three key constraints that a trade policy should fulfill in order to fit the situation in the Korean Peninsula: it should help to diffuse political tensions; it should take into account the profound lack of knowledge of the strengths and weaknesses of the North Korean economy in the world economy; it should be frugal in institutions since it will take time to build them in North Korea. Section 3 presents a first option, based on the remarkable success of the trade policy followed by the Baltic countries (Estonia, Latvia and Lithuania) or Georgia which are much better reference points for North Korea than Eastern Germany because their initial situation and problems were much more similar to those of today North Korea than Eastern Germany's. Section 4 presents an alternative option, followed by Chile, more progressive than the Baltics' policy but quite as much successful. Section 5 examines then the relative merits of a free trade agreement and a custom union between North and South Korea.

These three options require a *caveat*. They do not pretend to be exhaustive: they simply aim to launch a debate on concrete actions, in line with other papers [Chun and Rhee 2012]. They are a simplified presentation of the main alternatives for a North Korean trade policy, and they assume that decisions will follow economic logic. Of course, the reality will be much less simple and it will bring its load of unexpected events—economic and political. Compromises will be needed, goals adjusted and/or re-scheduled. However, these simple options offer very useful frameworks of concrete actions allowing to put isolated initiatives—such as the “internationalization” of the Gaeseong complex—in a global setting, to identify more easily and/or more rapidly deviations from an “ideal” trajectory, and, within those deviations, to recognize those which are essential to rectify and those which are not or with which one could work decently.

Section 1. Building trust needs concrete proposals

There is no doubt that the denuclearization issue is the top priority within the 3,500 kilometers around North Korea (that includes Guam but also most of China) as well as for the entire world in case of smuggling North Korean nuclear material to other chaotic countries. The problem is that this issue is so important that it tends to “freeze” all the parties involved in the Korean peninsula (a classical situation in case of nuclear threats). Nobody is ready to move because the costs and risks generated by a brutal collapse of the current North Korean regime are felt too high. As stated by Kim Jong Nam in his interview (the uncle of the current North Korean Leader living in Macau) “[...] *I personally believe that economic reforms and openness are the best ways to make life better for the North Korean people. However, taking North Korea’s unique position into account, there is a fear that economic reforms and openness will lead to the collapse of the present system*” [Lankov 2013, p.117].

“Freeze”...

This prevailing view of “no move now” relies on arguments which can be briefly summarized in terms of the main four actors in North Korea:

- the top nomenklatura is not ready to move because it fears that it will lose its current wealth and possibly its life in a transition process that it perceives as very fast at best, violent at worst, and any case uncontrollable.
- the lower ranks of the nomenklatura shares the same view—though with (possibly large) variations, depending on the extent to which these officials are truly protected from food crises, on how much money they earn by oiling the system via corruption, and also on how much they care about the rest of the population among whom they live (some officials have enforced laxly some of the policies decided by the top nomenklatura in order to protect North Koreans of the worst effects of these policies).
- the North Koreans running the officially blessed private businesses focus all their energy on consolidating what they have already achieved at such a great pain, and may be afraid of expanding their business in a more market-oriented environment.
- the rest of the North Korean population is probably mostly absorbed by the goal of surviving. The consequences on their welfare of the brutal reversals of North Korean economic policies during the last two decades may even have made them more

nostalgic of the Kim Il-sung era (the only memory they have of a period of acceptable and stable economic conditions) than of an unchartered market economy.

To make things even more difficult, the fear of a market-based future is, almost certainly, deeply entrenched in these four layers of the North Korean population. Of course, these fears have been fuelled by an intense propaganda during three generations now. But, more importantly, they have been magnified by North Korean policies which have associated (black) market-based successes to punishment: the 2009 brutal currency change was a spoliation of all the savings made in the previous currency unit by the North Koreans (except those of the top nomenklatura made in foreign currencies). It has been magnified by a devastating hyper-inflation which has hurt every North Korean—and sheds a light on the profound lack of economic understanding in the top nomenklatura.² Last but not least, black markets with no guarantees based on the rule of the law are better than empty shelves, but they have surely created countless frustrations among North Korean consumers.

or “Move”?

All these arguments make a lot of sense. Indeed, they describe a population and its ruling group exhausted by 70 years of an increasingly inefficient economic regime and by one of the strictest single party setting. That said, they do not eliminate the converse arguments that should often cross the mind of North Koreans and that would induce them to move forward.

These arguments could be briefly summarized as follows:

- the top nomenklatura can witness the fact that its peers in the other communist countries have well survived to the transition process. Those who have lost the power they used to have are now very wealthy by the North Korean standard and even often by the standard of their own countries under the communist rule. Since the fall of the Berlin Wall, none has lost his/her life in this process (with exception of N. Ceaucescu and his wife) in sharp contrast with the many violent deaths under the communist regimes. The danger to be part of the top nomenklatura is often under-rated in democracies while it is certainly very present in the mind of top North Koreans: life at the top of despotic regimes is full of fears, as amply documented by history from Han Wu-di to Stalin. Market-based and democratic countries are the only ones where being at the top does not run the systemic risk of being over-thrown violently.

² In a nutshell, it consisted in dividing prices by 100 while keeping unchanged wages. This was a sure recipe for a lightning hyper-inflation in a very poor country like North Korea.

- the rest of the nomenklatura can also hear about its equivalents in the other former communist countries, with some of them even running now their own countries (V. Putin being the best illustration). Very few members of the lower ranks of the nomenklatura have paid a sheer price for having been part of it: the hunts after the Eastern German Stasi or Romanian political prisons staff or the members of the Polish Communist Party have not gone very far (not to mention the amazing fate of some former KGB members).
- the managers of the officially-blessed private businesses have not had the same importance in the other communist countries than in North Korea: according to some estimates, roughly half of the North Korean food and basic consumer goods is produced and/or delivered by these managers [Lankov 2013]. Despite the absence of systematic evidence on the fate of these managers after the fall of the communist regime in other countries, it seems reasonable to guess that they have faced the usual fate of every business: the clever ones have adjusted to the changes and survived or prospered, the others have simply gone out of business.
- the rest of the Korean population have some hint—when they can get some news about the rest of the world—that they have little to lose because there are very few countries in the world as poor as North Korea.

Trust building: the need to talk concrete

Most of the North Koreans who have some time left to think about their future (and some access to information about the rest of the world) should thus be torn apart between these two sets of arguments. The number of these people may be not large, but it is probably large enough to trigger reforms and to support them if launched. What could thus be done for making the balance of arguments shifting from those favorable to the *status quo* to those favorable to change?

An attractive candidate seems to debate on concrete proposals—the key word being concrete—about every economic policy to be implemented during the transition period: what should and can be done, how fast, how wide, etc. The main goal of these debates is to provide enough information and options to the North Koreans for them to realize that the transition is not necessarily a fall into a chaotic and hellish world, but a reasoned and manageable shift to a more cooperative game via economic policy. Even if crude, concrete proposals have the

merit to give some ideas about the future, while improving the North Korean knowledge on economic issues. By contrast, keeping the debate on the economic future of the Korean peninsula to broad generalities cannot be conducive to such a trust because it leaves too much room to interpretations, fuelling the countless existing suspicions and leaving intact the existing fears.

In short, the primary role of these debates on concrete proposals is to build trust among all the parties of the Korean drama, including building trust among the North Koreans themselves on their own ability to move onto the transition path. This paper aims to contribute to only one of these debates—the one focusing on trade policy (of course, there should be similar debates on other economic policies).

Where to start the debates?

Under the present circumstances, the most likely place to start such debates is South Korea. But, that is not be specific to the Korean peninsula. Most of the debates on what could and should be done in Central Europe in the early 1990s started in Bonn (German reunification), Brussels (accession of the Central European countries) or London (covering the former USSR with the European Bank for Reconstruction and Development) before spreading to the Central European countries involved.

Indeed, rather than their initial location, what counts is the capacity of these debates to percolate into North Korea. This capacity is function of the abundance and quality of the options discussed, and their ability to attract the attention of the North Korean actors (the two nomenklaturas and the two peoples), and reduce the asymmetry of information between the two Korean economies.

The fact that such debates start in Seoul has an useful side. South Koreans are not immune to fears and suspicions on the future of the Korean peninsula. Instinctively, they realize that profound changes in North Korea will require efforts from them, possibly for many years. The German experience provides ample evidence that the reunification process can last much longer than initially thought. Still today, one does not need a lot of efforts to find in Eastern Germany buildings (situated on Karl Marx streets...) as decayed as those existing in the early 1990s, despite the billions of Euros spent by Western Germans. As a result, South Koreans

need to discuss the best possible concrete options from their own point of view among all those available.

Section 2. Three key constraints on trade policy

This section presents the three key constraints that a trade policy should fulfill in order to fit the situation in the Korean Peninsula. Firstly, it should make use of the potential of trade policy to diffuse international political tensions. Secondly, it should take into account the fact that there is so little knowledge on the North Korean economy, in particular once it will be connected with the world economy. Lastly, it should be frugal in institutions in order to accommodate North Korea's severe lack of institutions for some time in the future.

Making use of the capacity of trade policy to diffuse political tensions

A well designed trade policy has the interesting—rarely recognized—capacity to diffuse political international tensions [Ahnliid 2012]. This is best illustrated by the General Agreement on Trade and Tariffs (GATT) which, over its 47 years of existence (1948-1995) has deeply contributed to re-unite an economic world subjected to powerful centrifugal political forces, with the diverging tracks followed by the developed countries, the centrally-planned economies and the developing countries. In a similar (though more limited) way, the main benefit of a possible candidacy of South Korea to the negotiations of the Trans Pacific Partnership or of a Regional Comprehensive Economic Partnership (RECP) among many Asian economies is to get the benefits of freer trade while putting aside the political frictions existing among (some of) their candidate members—such frictions making bilateral trade negotiations much more difficult and risky.

The options examined in this paper use as much as possible this capacity of the trade policy to diffuse political tensions by insisting on a key WTO principle—the “most-favored nation” (MFN) which requires a country to impose the same treatment on imports from all the countries in the world. Sections 3 and 4 will make constant references to this requirement. Only the third option (section 5) deviates from such a rule by referring to a “preferential trade agreement” between North and South Korea—but, this is done in the perspective of the reunification of the Korean Peninsula.

The Gaeseong industrial complex provides a fascinating illustration of this capacity of trade policy to diffuse political tensions. In early 2013, the complex was in the eye of the storm, and the most extreme case of the political sensitivity that all bilateral trade agreements in the world can be subjected to [Messerlin 2013]. The recent decision taken jointly a few months later (in August 2013) by the North and South Korean authorities to “internationalize” the Gaeseong complex (see Box 1) is a huge step in using the above-described capacity of trade policy to reduce political tensions: involving other countries in Gaeseong will change dramatically the status of the Gaeseong complex by making it more “WTO-like”.

Box 1. Taking advantage of trade policy capacity to diffuse political tensions: the “internationalization” of the Gaeseong industrial complex

In August 14, 2013, South and North Korea agreed on the normalization of Gaeseong Industrial Complex (GIC) after 133 days of seizure. The joint declaration stated that no further closure of activities at GIC should occur by blockage of workers, or their retreat, and emphasized on the neutrality of the GIC from political tensions. In this joint declaration, the two parties have also agreed on concrete measures for internationalizing the GIC which would include (i) an active promotion of foreign enterprises in GIC, (ii) institutional reforms in labor, taxation, wages, insurance policies to international standard, (iii) the implementation of special tariff rate for exports to third country and (iv) an opening of a South-North joint Foreign Investment Fair.

<http://www.yonhapnews.co.kr/bulletin/2013/08/14/0200000000AKR20130814209200043.HTML>

In September 11, 2013, the second meeting of the South-North GIC Joint Committee, which was established by the Joint declaration on the normalization of GIC, has agreed on opening a common foreign investment fair for foreign enterprises in October 2013 in GIC. Such an “internationalization” process would require further elaboration on the side of the South Korean government by addressing institutional issues such as taxes and the possibility to make the goods produced in GIC recognized as products of South Korean origin in the context of the free trade agreements signed by Korea (for instance with the EU and the US). The Joint committee has also agreed on the composition of a “Commercial Arbitration Council” to serve as a dispute settlement body for disputes arising in GIC. The Commercial Arbitration Council was initially agreed in 2003 between South and North Korea, but it has not been put into practice.

<http://www.yonhapnews.co.kr/politics/2013/09/11/0505000000AKR20130911069153043.HTML>

Revealing the unknown North Korean comparative advantages

Designing a trade policy well adapted to North Korea faces a major challenge to an extent unknown in the rest of the world: there is very little valuable and trustable information on the North Korean economy which could help to guess its economic strengths and weaknesses (“comparative advantages” in economic jargon)—in short, the products that North Korea could produce and export successfully in the current world. Even the current trade flows (an information relatively easy to find for all the other countries in the world) are largely unreliable and hard to decipher. The large share of the North Korean trade with China in total North Korean trade (85 percent in 2011 [KIEP 2012]) is, to a notable extent, the result of circumventing sanctions (and, of course, these trade flows do not necessarily consist in Chinese products even if they transit via China).

The only certain information on the North Korean economy is that it is highly distorted and geographically very fragmented. Pyongyang is largely isolated from the rest of the North Korean territory, the regions close to the Chinese border are somewhat connected to China, while the transport infrastructure in the rest of the country is in such a terrible shape. Even, the current economic incentives delivered by the black markets are likely to be very different from those which would be provided by well-functioning domestic markets since these black markets operate under so peculiar transaction and transportation costs.

Such an unprecedented level of ignorance on an economy requires that all the instruments of trade policy to be used in the transition process should be primarily chosen for their capacity to eliminate progressively these existing distortions—in other words, for their capacity to reveal the “true” North Korean comparative advantages and, by the same token, to contribute to the economic reunification of the Northern Korean territory itself. Sections 3 to 5 will make frequent references to this requirement.

A trade policy “frugal” in institutions

The abundant literature on North Korea makes clear that key pillars of a modern trade policy are not present in North Korea: very little trust among foreign and North Korean traders [Haggard, Lee and Noland 2011], distorted markets dominated by rents fuelled by official monopolies or officially-blessed black markets [Lankov 2013], no institutions but the rule of volatile personal relations (and trade alone does not create institutions [Haggard and Nelson 2013a and 2012b]).

This situation raises a key problem because a modern trade policy often relies on a vast array of elaborated institutions—from sophisticated Customs Office to the many regulators in services to the agencies or committees enforcing tests and certifications of norms to the administrations implementing contingent protection instruments (antidumping or safeguard cases), etc. All these institutions cannot be created from scratch within a few years, or even within a decade for many of them. There is thus a need to look for trade policy options which minimize the recourse to institutions or which can have recourse to simpler and more easily available substitutes.

Section 3. Option 1: the fast transition of the Baltic countries and Georgia

Developing concrete proposals is easier if one has some good reference points to look at. The literature on the Korean reunification refers generally to the German experience—probably because of the reunification dimension. However, this reference is not appropriate from both an economic and political perspective.

- from an economic point of view, Eastern Germany was in 1989 one of the best run economies in the Soviet Union's block. Its GDP per capita amounted to 43 percent of Western Germany's GDP in 1991. By contrast, the North Korean GDP per capita in 2011 is estimated to be 6 percent of the South Korean GDP per capita (1800 USD vs. 32000 USD at PPP rates [CIA 2013]). Moreover, the Eastern German economy relied on an infrastructure which was still operational, even if it were ageing rapidly due to a lack of investments. If corruption was high as in any centrally-planned economy, it remained within acceptable limits.
- from a political perspective, it became rapidly clear that Soviet Union, then Russia, would not interfere with German reunification. There were compelling reasons for such a hands-off behavior: Russia became absorbed by its own transition problems, had no enough financial resources to intervene, and had to recognize its decline as a world super-power. China is in a very different economic, financial and political situation.

In fact, there is only one useful lesson from German reunification. Despite the much better initial economic and political situation than the one prevailing in the Korean peninsula and a booming world economy in the early 1990s, the German integration process is still a work in

progress 23 years later. In 2011, the Eastern German GDP amounted to 71 percent of the Western German GDP per capita—a gap big enough to still feed some nostalgia of the communist era among some Eastern Germans [Scharioth 2012].

A much more appropriate reference: the Baltics and Georgia

A much more useful source of inspiration for the North Korean case is provided by the Baltic countries (Estonia, Latvia, Lithuania, or Baltics) or by Georgia.

- The Baltics were as poor (Estonia) as or even poorer (Latvia) in the early 1990s than North Korea today, and they faced the same level of economic and political uncertainty than the one prevailing in the Korean Peninsula today: very little idea about their comparative advantages, a more fragile international situation because Russia was less ready for a stand-off policy with respect to former members of the USSR, all the more because the share of Russians in the populations of the Baltics ranged from being notable (Lithuania) to substantial (Estonia and Latvia).
- Georgia faced the same constraints (still does) even more severely. In 2004, it was as poor as North Korea today, with huge economic distortions (being Stalin's homeland was not helpful) and corrupted (Georgia was seen as the most corrupted Soviet Republic in the USSR). Russia has been persistently unfriendly to the point of generating the secession of Abkhazia and South Ossetia. To make things worse, Georgia's economic situation deteriorated during the first years of independence because the transition process was initially poorly managed. Despite all these negative factors, Georgia's situation improved dramatically within a couple of years under the first Saakashvili Administration (2004-2008), with Georgian GDP per capita reaching 3,000 USD in 2008. As a result, sections 3 and 4 make references to the Saakashvili's trade policy of this time.

The early 1990s have witnessed a frenzy of debates on concrete plans for Central European countries. Initially, these plans focused on the international security aspects, particularly on the accession to NATO. When this goal was perceived out of reach in the short run, the debates shifted to the best NATO substitute—the EU and the economic domestic policies to make possible EU accession. A crucial outcome of these debates was to reveal how wide the range of possible policies was—from fast to progressive transitions. Indeed, the current 11

Central European EU Member States under a communist regime until the 1990s did chose very different accession paths.

The Baltic and Georgian trade policy choices: a fast transition

The Baltics have favored relatively radical choices—in trade policy as well as in other economic policies—Estonia being the most extreme and consistent in this matter, and Georgia has followed their examples after 2006. Table 1 summarizes these policies. It shows that a fast transition trade policy consists in very few measures:

- the elimination of almost all the tariffs and tariff-equivalents (licenses, quotas, etc.) on both imports and export (in the European centrally-controlled economies, barriers to exports were often as constraining as barriers to imports).
- a very short list of exceptions (5% of the products in Latvia) largely concentrated on agricultural products and on the export side.³
- the abolition of state trading.
- the currency regime, that is, how easy it will be for traders to find foreign currencies at a good rate.⁴

It is interesting to note that all these measures were very frugal in terms of institutions. There was no or very little need of administrations for granting licenses and quotas, and the role of the Custom Offices was quite limited since a vast majority of goods were subjected to the same tariff rate (anyway too low to trigger corruption). If one wants to characterize this policy, it was a policy of an almost uniform and MFN tariff—uniform meaning that the same tariff rate was imposed on all the goods—with a tariff rate close to zero.

These measures were sometimes qualified as “shock therapy”. But, this term does not describe well the trade policy of these countries for two reasons:

- in fact, the Baltics and Georgia were producing very few products (in the USSR, productions were allocated among the various Soviet Republics by central planners

³ There are roughly 6,000-7,000 products in a trade tariff structure defined at the HS-6 digit.

⁴ The foreign exchange measures are crucial, but they are not discussed in this paper because they are much more tightly related to the broad monetary and budgetary policies than to the trade policy *per se*.

much more concerned by political inter-dependency than by economic efficiency), and the production of most of them was undoubtedly unsustainable in a non-distorted economy. In other words, eliminating most of the tariffs was either concerning goods never produced or goods visibly inadequate with respect to the countries' comparative advantages.

- export constraints were limited to few products—an important limit since barriers on exports are equivalent to barriers on imports, hence can re-introduce a substantial dose of protection if they are many.

Table 1. Key components of trade policy reforms: the Baltics and Georgia.

	Estonia	Latvia	Lithuania	Georgia [a]	
Import restraints	Tariffs	0.5% for statistical purpose.	Average tariff of 10%, low rates on inputs.	Unweighted average of 3.2% with a 0-30% range; 75% have a zero tariff; inputs have low rates.	average tariff of 1.5%, 85% tariff lines are duty free, the rest has a 12% tariff.
	Licenses and quotas	None.	No licences, but specific duties on 150 products (defined at HS-6 digit).	About 10 products.	None.
Export restraints	Taxes	Taxes for cultural items only. 0.5% on other items.	383 tariff lines (defined at HS-6 digits) subjected to 1 to 100% export taxes, with 90 percent of them below 10%. Mostly agricultural products, metals, raw materials (sands, wood, leather).	15 products (defined at HS-4 to 5 digits) subjected to export taxes ranging from - to 50%, with 90% of them below 10%.	None.
	Licenses and quotas	Tobacco, alcohol, some agricultural and forest products, metals, broadcast equipment, oil shale, petroleum and mineral oil.	None.	None, except for temporary bans on red clover seed, untreated oak and ash timber.	Minimal export restrictions (health, environment, culture).
State trading	None.	None.	None.	None.	
Foreign exchange	Convertible current account with a currency board mechanism since 1992; no surrender requirement since early 1994; virtual capital account convertibility.	Convertible with wide access to foreign exchange through commercial bureaus; no surrender requirement.	Convertible since 1992; currency board since April 1994; no surrender requirement.	Floating exchange rate.	

Source: For the Baltics: Michalopoulos and Tarr [1996]. For Georgia: WTO Trade Policy Review [2010].

Table 2 shows the GDP growth of all the Central European countries having joined the EU—hence having also benefited from the same support from the EU (Georgia is not included in Table 2 because it has faced (still facing) such a different international environment, including war). It shows clearly that, over 18 years, the growth performance of the Baltics has been better than the growth performance associated to more progressive trade policies implemented by other Central European countries.

Table 2. GDP per capita of the Central European EU Member States, 1995-2013

	Growth rates (%)				GDP per capita			
	GDP per capita		GNI per capita		current \$		Slovenia=100	
	current \$	PPP [a]	current \$	PPP [a]	1995	2012	1995	2012
Baltic countries								
Estonia	12.2	8.1	n.a	7.8	2629	16316	25.0	73.9
Latvia	12.3	8.2	11.9	8.2	2107	14009	20.0	63.4
Lithuania	12.6	8.3	12.0	8.0	2178	14150	20.7	64.1
Other Central European EU Member States								
Bulgaria	11.9	6.6	10.4	6.6	1555	6986	14.8	31.6
Croatia	9.3	5.8	6.6	5.6	4722	13227	44.9	59.9
Czech Republic	9.0	4.4	11.5	3.9	5596	18608	53.2	84.2
Hungary	7.1	5.3	6.9	5.0	4411	12622	41.9	57.1
Poland	9.4	6.7	9.1	6.5	3603	12708	34.2	57.5
Romania	11.7	7.2	11.7	7.1	1564	7943	14.9	36.0
Slovak Republic	9.4	6.8	10.1	6.7	4710	16934	44.8	76.7
Slovenia	7.2	4.7	6.9	4.5	10524	22092	100.0	100.0

Note: [a]: PPP: purchasing power parity. Source: World Bank

Section 4. Option 2: the more progressive transition of Chile

The Baltics and Georgia trade policies may be seen as a too bold jump for North Korea. After all, even under the USSR rule, the Baltics and Georgia had many more and much more diverse economic relations with the rest of the world than those that North Korea is having today. What then could be the main features of a more progressive trade policy which could be successful enough to create an economically sound momentum? Four features emerge as essential.

4.1. Keeping an uniform and most-favored nation-based tariff

The early 1990s Baltic trade policies boil down to three key elements:

- they impose the same tariff rate to all the countries of the rest of the world: in short, they follow the most-favored nation (MFN) principle;
- they impose the same tariff rate to (almost) all the products: in short, they were imposing an (almost) “uniform” tariff.
- they impose an uniform and MFN tariff rate equal or close to zero.

The mid-2000s Georgian trade policy followed the same strict MFN principle; but its tariff schedule was slightly less uniform (with a notable number of tariffs of up to 12 percent).

If North Korea wants a more progressive but still economically sound trade policy, it should keep the two first principles—uniform and MFN—and redefine the third one—the zero or close to zero rate. What follows summarizes the arguments behind such a choice and presents the very successful case of the country which has made such a choice—Chile.

Keeping an uniform and MFN tariff is driven by the fact that North Korea’s comparative advantages in the future are unknown. Today North Korean economy is so much distorted by domestic and foreign conditions that there is almost no clue on the products that the North Korean economy could successfully produce and export to the rest of the world—if one excepts some rare minerals [Bruce 2012]. Looking at past North Korean exports is of no help. Until the 1980s (when the North Korean economy was still in a not too bad shape) North Korea’s comparative advantages have been in industries such as coal and steel which are characterized today by over-investments in the world, hence should be avoided.

An uniform and MFN tariff higher than zero on all the imported goods remains the best instrument to reveal North Korea’s comparative advantages for the following reasons:

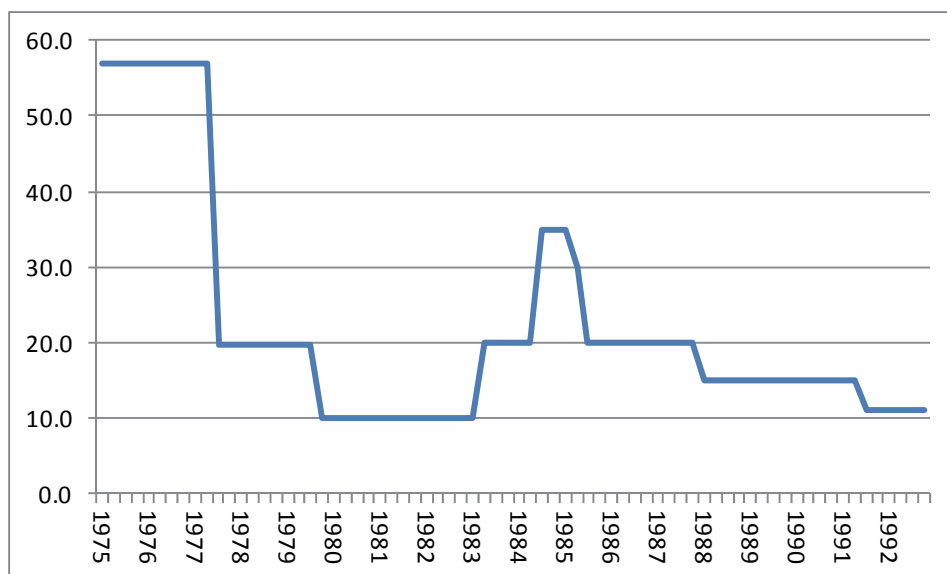
- investors (large and small, foreign and domestic) will not be induced to invest in certain North Korean sectors because they are the most protected ones. For instance, they will not be induced to invest in a product A in which North Korea has no comparative advantage but which is protected from foreign competition by a high tariff of (say) 30 percent—instead of investing in a product B in which North Korea has no comparative advantage but which is protected only by a low tariff of (say) 10 percent. Protecting all the products by the same MFN tariff will induce all the

producers to invest in the products only on the basis of the economic potential of these products.

- because of its “neutrality”, a uniform and MFN tariff is the most favorable tariff structure for a fast diversification of the domestic economy because investors’ decisions will not be slowed down by a rigid tariff structure (changing tariffs is a daunting task because it tends to mobilize all the powerful lobbies in a country) hiding the (possibly fast) evolving comparative advantages of North Korea. Diversification will boost confidence in North Korea economic potentials among the domestic or foreign investors. It is one of the most powerful forces to attract foreign investors with fresh ideas.
- last but not least, such a neutrality reduces considerably the risks of corruption in the Customs administration. This factor is crucial for making North Korea an attractive place for investors. It is also crucial since tariff revenues will be the main source of domestic fiscal resources in North Korea for the first decisive years of transition. Georgia offers a good illustration of the fast impact of a (relatively) uniform and MFN tariff policy in this domain: in less than four years, Georgia shifted from the 133th most corrupted country (in 2004) to the 66th (in 2009)—achieving a better rank than some EU Member States [Transparency International 2012].

As economic analysis shows [Tarr 2000], arguments against a uniform tariff are related to terms of trade effects, “strategic,” infant or restructuring industry considerations, revenue or balance of payments purposes, and tariffs as a negotiating tool at the WTO. None of these arguments are important for North Korea at the beginning of its transition. Terms of trade effects and strategic industries assume that North Korea would enjoy market power in some world markets, a very unlikely situation. Infant or restructuring considerations are precisely those that should be avoided because of the deep level of ignorance about North Korea’s comparative advantages. Revenue or balance of payments problems are better handled by macro-economic policies. The case of the WTO is addressed below (see section 4.3).

Figure 1. The history of the uniform tariff in Chile, 1979:1-1991:4 (trimester basis)

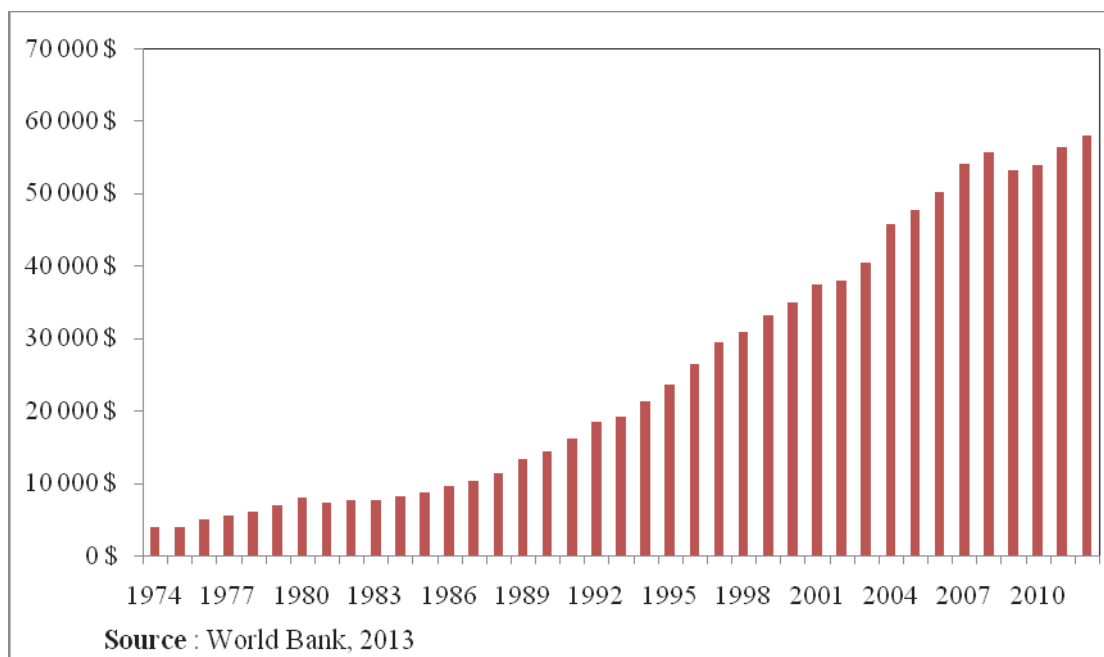


Source: Corbo, 1997

Chile is the best illustration of how an “uniform, MFN and non-zero” tariff policy can boost growth and diversification, and how to manage such a policy in detail [Corbo 1997]. In 1973, Chile’s average tariff was 105 percent (with many peaks as high as 750 percent, combined with many quotas and a multiple-exchange rate system). In 1975, the average tariff was still 57 percent, as shown in Figure 1. The Chilean government was already talking about an uniform and MFN tariff rate of 10 percent, but it took four years to reach this target. However, this move did not work well: domestic and foreign investors did not realize the benefits of such a solution, hence lobbied heavily against it, and the economic crisis of 1982-1984 forced the Chilean government to backtrack, increasing the tariff rate first to 20 percent and then to 35 percent. But, crucially, the tariff was kept uniform.

In March 1985, the Chilean government started again to cut the tariff to 30 percent. Domestic producers began then to realize that the level of the uniform tariff had no real impact on their investment decisions since all domestic prices were 30 percent above the world level, with no product being treated more favorably than the others. As a result, despite the shift to a democratic regime, there was no opposition to a subsequent series of tariff cut from 30 percent to 11 percent between 1985 and 1992 (today, the Chilean uniform and MFN applied tariff is 6 percent). Remarkably, since then, the private sector has been demanding of these further tariff cuts which were often decided unilaterally by Chile.

Figure 2. Chile’s exports of goods and services, 1974-2012 (2005 constant US dollars)



The reason behind such a change of mind was that, as illustrated in Figure 2, Chile witnessed a take off (unabated since then) of its exports and a fast diversification of its export structure—from overly dominant exports of copper to a much more diverse export structure, including with many farm and food products.

The key question is then: at which initial level should the uniform and MFN tariff rate be then fixed? The above-reported history of the Chilean tariff policy case provides a crucial lesson: what counts is not hastiness, but perseverance. In fact, an initially low uniform tariff runs the risk to be misunderstood (businesses are obsessed by the “low” feature and do not pay attention to the “uniform” feature) to the point to generate political failure. That said, how high is “high”? In the North Korean case, the initial tariff level should take into account two considerations:

- the higher the initial uniform tariff is, the stronger the pressures for getting exceptions are likely to be, undercutting the whole rationale of the uniform tariff policy,
- it would be harmful to impose a tariff higher than the level of protection currently prevailing *de facto* in the North Korea economy. With the collapse of the North Korean system of centrally-planned distribution, most goods are supplied and purchased on “grey” markets. This situation can be analyzed as equivalent to a myriad of different local “tariffs” on the imported goods all over the North Korean territory. The level of these tariffs depends on the local costs of the risky import business: the local corruption costs, the super-profits that local traders want to get, the level of local

competition, etc. For preparing the transition, it would thus be useful to collect a good range of these grey prices all over the North Korean territory in order to have the best idea possible of these implicit local tariffs.

- the North Korean uniform tariff should not be above the highest South Korean tariffs in order to prepare the Korean reunification process from the start of the reforms. In manufacturing, the highest South Korean MFN bound tariff is 35 percent (textiles, minerals, all products which indeed may have a future in the North Korean economy) while the highest South Korean MFN applied tariff is 16 percent.⁵

Depending the result of the study on grey prices in North Korea, the possible initial uniform tariff rate for manufactured goods could then range from 16 to 35 percent at most. A tariff within such a range should give enough breathing space to domestic and foreign investors for discovering the products in which North Korea has comparative advantages. As and when the North Korean economy will improve, this initially high uniform tariff should be reduced—but always in the uniform way.

4.2. Free Economic Zones (FEZs)

The problem of a high uniform and MFN tariff is that it makes expensive the inputs and machines that North Korea will need to import massively in order to start and develop its new productions. A first solution to this problem is a system of drawbacks (whereby duties on goods utilized in the production are given back to the importers-producers) which has been routinely used by South Korea. But, such a system requires skilled, efficient and uncorrupted Customs Office—an institution that South Korea has now, but that will take years to build in North Korea.

A much simpler solution are the FEZs which are well defined territories devoted to production in which goods can be imported from the rest of the world at a zero (or very low) tariff—hence by definition immune to the disincentives generated by an initially high uniform MFN tariff. They are an attractive solution for North Korea for three reasons:

- it is a structure well known by North Korea which, as shown by Figure 3, operates four FEZs: Gaeseong on the border with South Korea, Rajin-Sonbong (“Rason”) on the border with Russia, Sinuiju and Hwanggeumpyong on the border with China.

⁵ There are exceptions in the chemical sector, as shown by Table 1. The agricultural sector is examined below because the maximum South Korean tariffs are extremely high (from 300 to 900 percent).

- FEZs offer an efficient solution to another huge North Korean problem: its severe lack of infrastructure. It will take time to build all the roads and railways that would be necessary for industrializing the whole North Korean territory. FEZs on North Korean coasts minimize the immediate and heavy requirements in terms of infrastructure. Instead of shifting goods and equipments to every part of the North Korean territory, it relies on the much less expensive and faster to implement movement of North Korean labor to the FEZs.
- As FEZs require swift and accurate customs controls, they need efficient Customs authorities. Being limited areas of the North Korean territory, FEZs could benefit from the support of the South Korean Customs administration which is one of the most efficient Customs in the world.

Figure 3. The existing FEZs in North Korea



Finally, FEZs have the capacity to generate two dynamic processes extremely helpful for a successful transition:

- they will exert a pressure to reduce the initially high uniform MFN tariff adopted for the rest of the North Korean territory. The co-existence on the North Korean territory of FEZs (with a zero uniform tariff) and of the rest of the territory (with an initially high uniform tariff) will inevitably generate smuggling if it lasts long (all the more because of the long tradition of smuggling in North Korea). The only way to manage

this risk is to reduce progressively the initially high uniform tariff in the North Korean territory not devoted to FEZs.

- FEZs would not be able to play fully their role of driving export forces if they are not part of the network of the preferential trade agreements built patiently by South Korea during the last decade. This is not the case today. For instance, goods produced in the Gaeseong complex are excluded from the coverage of the current free trade agreements between South Korea and the EU or the US—hence not eligible for the zero tariffs that South Korean goods can enjoy in the EU or US markets. As stressed in Box 1, the “internationalization” of Gaeseong has the explicit objective to make the goods made in Gaeseong eligible to the status of goods from South Korean origin in the preferential trade agreements involving South Korea.

For all these reasons, creating more FEZs in North Korea is an efficient measure to combine with a initially—but decreasing over time—high uniform MFN tariff for the rest of the North Korean territory.

4.3. Accession to the World Trade Organization (WTO)

The accession of North Korea to the WTO is legally possible for North Korea under the status of a “customs territory”. Such a status is almost certain to be granted if North and South Korea decide to take the same approach than Taiwan (or Hong Kong and Macau) and China Mainland, for instance.

That said, would an accession of North Korea be desirable from an economic point of view? What has happened to all the countries acceding to the WTO suggests some caution. Since 1995, the accession process has become a tough one by which the WTO Members of the *ad hoc* North Korean accession committee are using their negotiating leverage to extract the maximum concessions from the candidate country. North Korea was the industrial power house of the united Korea in the first half of the 20th century, and this situation has continued until the 1960s-early 1970s. The trading partners of North Korea will have this history in minds when negotiating the North Korea’s accession, and they should be expected to have very demanding requests for concessions. Moreover, some of these requests could have some consequences on South Korea’s trade regime in case of a custom union between North and South Korea (see section 5) and in case of reunification.

By contrast, getting quickly an observer's status at the WTO seems highly desirable since it would allow North Korea to improve its knowledge of the world trading rules.

4.4. The case of agriculture

Most of the exceptions to the close to zero uniform and MFN tariff adopted by the Baltics were concentrated in agriculture (and in some raw materials) under the form of export quotas. Chile has also somewhat protected its farm sector, but only by adopting special safeguard procedures relatively easy to trigger in case of surge of imports of farm products (Chile did not take equivalent procedures for the industrial goods). Should North Korea follow the Baltic or Chilean examples? Certainly not the Baltic case, and with great care the Chilean precedent, if one accepts the following arguments.

A large share of the North Korean population is still working in the farm sector. But, this is partly because there is no free movement of labor in North Korea (and a weak demand in industry) partly because North Korea is using inefficient farming techniques. Successful FEZs will attract young North Koreans living currently in the rural areas because they will find better incomes and life conditions than in their rural regions. This emigration will have two impacts on the North Korean rural population:

- the number of young farmers will shrink rapidly. This evolution would make easier the modernization of the North Korean farm sector that should be encouraged on the basis of the world prices, and not be artificially protected by tariffs different from the one applied on industrial products.
- the whole rural North Korean population would be ageing rapidly. This second evolution makes both attractive and easier the adoption of a modern farm policy early in the transition process. Modern farm policies are based on direct income support to farmers—avoiding by the same token the trap of tailor-made high tariffs on the imports of farm products (as illustrated by many countries, including South Korea). Three factors would limit the budgetary costs of a modern farm policy in North Korea: (i) income support will need to be implemented only when the initially high uniform MFN tariff will be start to be cut substantially; (ii) it should be set at a level that would not slow down the desirable labor migration from rural areas to FEZs, and (iii) a “true” income support should be granted specifically to every individual farmer (if it is

not the case, income support becomes a never-ending land subsidy, blocking any evolution in the farm sector). Hence, it should target first and foremost the old farmers who would have too hard time to adjust to the new farming techniques.

Section 5. Looking at reunification path

The Baltics have joined the EU and its custom union. Chile has negotiated free trade agreements (FTA) with a notable number of countries. All these cases show that the uniform MFN tariff policy can be seen as an efficient transitory policy first for opening the economy to the world and then for preparing it to deeper relations with some countries. What could be the pros and the cons of FTA and custom union in the context of the reunification of the Korean Peninsula—a point already examined by Chun and Rhee [2012]?

This question echoes to some extent a political debate on the relations between North and South Korea that can be traced back to President Kim Dae-Jung's visit to North Korea and to the 6.15 North-South Joint Declaration in June 2000. This debate could be briefly summarized as a choice between a confederation and a federation—though this choice could evolve over time (confederation first, then federation). A free trade area is basically “confederalist” while a custom union can have some (light or strong) “federalist” tone. In many respects, the EU was completely confederalist in its early years (consensus for every decision) and, over time, has taken a more federalist tone when some decisions have progressively be taken under the (weighted, then simple) majority rule.

5.1. A free trade agreement (FTA) between North and South Korea

In this case, North Korea will make an exception to its uniform MFN tariff by eliminating its uniform tariff on South Korean goods only. There are three options for dismantling the intra-Korean tariff barriers:

- the first one (used by the EU in its early years 1958-1969) consists in a cut of an equal percentage every year over a given period (a 10 percent annual cut in the EU case);
- the second option has been much debated during the Doha Round: it consists in applying a ‘Swiss’ formula which would cut the higher tariffs by a larger percentage than the smaller tariffs. This second option could only be implemented by South

Korea since the North Korean tariff is uniform: its advantage is that it accelerates North Korean market access to the South Korean markets;

- the third one could be an asymmetrical tariff dismantlement, whereby South Korea would eliminate all its tariffs (not only the highest ones) faster than North Korea.

That said, today FTAs aim to address all the other major trade issues confronted by a modern economy, such as industrial norms, regulations in services, intellectual property rights, public procurement, state-owned enterprises (SOEs), etc. These so-called “21st century” trade issues are much more challenging than mere tariff cuts, and the FTA between North and South Korea should pay attention to two aspects—one from the North Korean perspective, the other one from the South Korean perspective.

The North Korean perspective. The FTA should not overburden the initially limited and fragile institutions in North Korea, nor the North Korean population which will remain too poor for a long time for being ready to pay for many aspects of a modern economy (such as environmental norms). The right balance could be achieved in two different ways:

- an unique FTA text could cover the whole range of issues in an ambitious way, but its schedule of implementation at least on the North Korean side would be designed with great care in order to take into account North Korea’s capacities to absorb or deliver the FTA provisions. The EU took this approach in its early years. The Treaty of Rome has the deepest and widest set of provisions covering all the topics conceivable in the late 1950s. But its implementation was very progressive: ten years for dismantling the intra-EU industrial tariffs starting in 1958, ten years for crafting and fully implementing an agricultural policy starting from 1964, slow and still incomplete elimination of the non-tariff barriers starting in the late 1960s, the still unfinished agenda of services liberalization starting in the late 1980s, etc. Unfortunately, the EU forgot this careful approach when it included additional Members States—putting too much burden on some of them (from Greece to Romania to Cyprus) with the consequences revealed by the 2008 Financial Crisis.
- Alternatively, the FTA between South and North Korea could follow a tradition more frequent in Asia. It would consist in a series of FTA texts negotiated over time and covering more and more domains in an increasingly deep manner. The best illustration of this approach is the Economic Cooperation Framework Agreement between China Mainland and Taiwan.

The South Korean perspective. It is important to stress that concluding a FTA with North Korea would also be demanding to South Korea. In particular, it would require an internal in-depth evaluation of the intrinsic quality of the regulations enforced in South Korea in order to assess which ones are good enough to be included in the FTA and which ones should be revised before any inclusion in the FTA (as best illustrated by the South Korean agricultural policy).⁶ It is a great pity that this fully fledged regulatory assessment programme has not been done in the EU before the accession of the Central European countries. This absence of assessment has forced these countries to adopt hastily a huge amount of unrevised regulations (in one case, the Polish Parliament adopted some 150 new laws in one package) which happened to be often much too expensive for their level of income. And, it has left the Western EU Member States with out-dated regulations the consequences of which are still visible in today EU economic performance.

5.2. A custom union between North and South Korea

The alternative to FTA would be a custom union between North and South Korea. A Korean customs union would not be much different from a Korean FTA except in two respects.

First, the custom union requires that North and South Korea will adopt the same tariff with respect to the rest of the world. This is not simple matter because the current South Korean tariff structure is very different from the EU tariff structure at the time of Eastern Germany accession—in fact, it is much less capable to reveal the North Korean comparative advantages than the EU tariff structure of the early 1990s.

As illustrated by Table 3, South Korea has often higher average and peak applied MFN tariffs than the EU. It has also a wider range of MFN tariffs (with peaks two to three times larger than EU tariff peaks), and much larger differences between applied and bound tariffs (“tariff water”) than the EU.⁷ Of course, the PTAs signed by South Korea (such as the Korea-EU or the Korea-US trade agreements) means that, on average, the South Korean tariff structure is

⁶ Such a process would enormously benefit from the creation in Seoul of an institution such as the Australian Productivity Commission which would be asked to review the South Korean regulations.

⁷ That said, South Korea has the KOREU and KORUS PTAs—that is, counter-forces to protectionist incentives to increase South Korean applied tariffs up to the bound level in order to solve transition problems in NORTH KOREA.

de facto much closer to zero than shown in Table 3. But, the MFN tariffs are those which count, and South Korea has no PTAs with many countries—among them China and Japan which are critical sources of cheap products (for the poor North Korean) and of equipment (for industrializing North Korea).

The non-uniform feature of the South Korean MFN tariffs is much less capable to reveal the North Korean comparative advantages than the EU tariff structure which was much closer to an uniform MFN tariff (if one puts aside the agricultural products). Consequently, a Korean customs union would put pressure on South Korea to substantially and unilaterally ‘flatten’ its existing MFN tariff schedule in order to help North Korea to better realize where lie its comparative advantages.

Table 3. Tariff structures of South Korea and the EU

	South Korea					European Union				
	Final bound duties			MFN applied		Final bound duties			MFN applied	
	avg	max	bound	avg	max	avg	max	bound	avg	max
Animal products	26	89	100	22	89	24	140	100	23	140
Dairy products	70	176	100	68	176	58	226	100	55	205
Fruits, vegetables	64	887	100	58	887	10	170	100	12	170
Coffe, tea	74	514	100	54	514	0	25	100	6	25
Cereals and prepa.	161	800	100	134	800	20	167	100	16	167
Oilseeds	44	630	100	37	630	7	171	100	7	171
Sugar	32	243	100	17	243	28	131	100	29	131
Beverages	43	270	100	32	270	22	175	100	19	162
Cotton	2	2	100	0	0	0	0	100	0	0
Other ag. products	21	754	100	16	754	4	131	100	5	131
Fish	15	32	54	16	47	11	26	100	10	26
Minerals, metals	8	35	96	5	8	2	12	100	2	12
Petroleum	9	13	80	5	8	2	5	100	3	5
Chemicals	6	373	98	6	317	5	17	100	5	17
Wood, paper	3	13	89	2	10	1	10	100	1	10
Textiles	17	30	99	9	13	7	12	100	7	12
Clothing	28	35	100	13	13	12	12	100	12	12
Leather, footwear	12	16	98	8	16	4	17	100	4	17
Non-elec. Machinery	10	20	97	6	13	2	10	100	2	10
Elec. Machinery	9	20	74	6	13	3	14	100	3	14
Transport equip.	8	20	81	6	10	4	22	100	4	22
Manufactures, nes	10	16	95	7	13	3	14	100	3	14

Note: For simplicity sake, figures have been rounded. [Source](#): WTO website, Tariff profiles.

Turning from producers to consumers, the South Korean tariff structure raises another important question: to which extent the current South Korean tariff structure protects more the “cheap” goods than the luxury goods? If it taxes more the cheap goods than the luxury goods,

the custom union may well be more favorable for the goods consumed by the North Korean “upper-class” at the detriment of those demanded by the average North Koreans. That could only create political problems: a smooth road towards reunification requires a strong support among the population, and above all among the (very) poor people—echoing a core aspect of the “Han River miracle”, namely the minimal differences among the various layers of the South Korean population.

The last consequence of a custom union between North and South Korea is that North Korea would automatically “join” the WTO with the same concessions and obligations than South Korea. This would be similar to what happened to Eastern Germany (Estonia and Latvia acceded to the WTO in 1999 and Lithuania in 2001, that is, before their accession to the EU in 2004). By becoming part of the Federal Republic of Germany, a EU Member State, Eastern Germany was immediately subjected to all the WTO concessions and obligations of the EU—from tariffs to industrial norms to sanitary and phyto-sanitary measures to trade facilitation to intellectual property rights, to public procurement, etc. In this respect, a customs union would be less flexible than a FTA, and would be much more demanding on North Korea.

Concluding remarks

This paper provides three simple but consistent options for designing a trade policy well suited to the Korean Peninsula: a fast transition (like the Baltics or Georgia) a more progressive transition (like Chile) and the choice between a free trade agreement and a custom union in the reunification perspective. All these options fit key constraints—the need to diffuse political tensions, to reveal the North Korean comparative advantages and to be frugal in terms of institutions. They are friendly to free economic zones—the internationalization of the Gaeseong Industrial Complex fits very well these frameworks. Last, but not least, the recent history shows that all these options have contributed to outstanding economic successes of countries which have gone through difficulties very similar to those faced by North Korea.

Of course, trade policy is only one element of the reforms to be made. Exchange rate policies, structural policies (such as state-owned enterprises), etc. are also decisive for shaping economic success. These crucial topics should also be debated in order to reveal the wide

choices in terms of concrete measures—illustrating that the transition period is not a shift to a chaotic world if it is well managed.

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